88-1517

Supreme Court, U.S.
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Docket No. _____

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In the Supreme Court of the United States

In the Term of the Court for 1988-9

On Appeal from the United States Court of Appeals For the Fourth Circuit in Case Number 88-2074

ROBERT SCOTT DUNNING,
Petitioner-Appellant
v.

COMMISSIONER OF INTERNAL REVENUE,
Respondent-Appellee

Jurisdictional Statement

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33 pp

I

Questions Presented

The case which taxpayer petitions for re-examination involves the IRS disallowance of business deductions for an artist in the early years of his business under Section 183 of the tax code, in which the taxpayer argues that the IRS improperly and arbitrarily classified the business as a hobby when it was actually a serious business and professional activity. This petition is respectfully submitted to the Supreme Court to raise the following issues:

1. The Appeals Court premised its decision on the assumption that the Statutory Notice of Deficiency supplied by the IRS in the case was "presumptively correct" and that the Tax Court had upheld

the presumptive correctness of this document. The Tax Court itself rejected the presumptive correctness of the IRS Notice of Deficiency. The requirements of the law under Section 183 of the U.S. Tax Code are questioned with respect to the validity of a Statutory Notice of Deficiency and the associated presumptive correctness of such a notice absent due diligence by the IRS in issuing the notice and in the total absence of any attempt to support the notice before the Tax Court.

2. The position of the Tax Court which the Appeals Court has now affirmed, if allowed to stand, results in an inconsistency in the application of the law under Section 183 setting a different standard of compliance with this law between different taxpayers and between taxpayers and the IRS. The present ruling raises the question of whether IRS and the

Tax Court are exempt from compliance with the major provisions of the tax code while at the same time setting an arbitrary and, in the instant case, impossible standard of compliance for the taxpayer.

3. A Constitutional question is involved in this case with respect to Article II, Section 3. of the Constitution of the United States which requires the president, and therefore the Executive Branch which includes the IRS, to "...take Care that the Laws be faithfully executed,..." The question before the Court in this case is whether agencies of the Executive Branch are required to honor the major provisions of the laws they administer by mandate.

4. An important issue is raised as to whether a court is required, absent any extaordinary circumstance, to base its

rulings on the case that is actually presented to the court by the litigant, and particularly a federal agency, or whether, absent such circumstances, the court is empowered to substitute a case of its own invention and then to rule on the substituted case.

5. A question is raised with regard to orderly proceeding in court cases. The question raised here is whether a court judgment can do service for a required administrative judgment of an agency of the Executive Branch when the executive agency has failed to bring a proper case under given legislation by willfully failing to observe the precepts of that same legislation.

6. With regard to the previous item, a Constitutional question is involved under Article V of the Bill of

Rights which requires due process of law before property can be taken from any citizen for public use. The question here is: Does mere accusation by the IRS without compliance with Congressionally mandated procedures constitute due process?

7. A question of uniform administration of justice is involved with respect to the "presumed correctness" of a Statutory Notice of Deficiency which is fundamental to the administration of the Tax Code. If the opinion of the Tax Court in the instant case is allowed to stand; then newly enacted legislation with regard to the "Taxpayer's Bill of Rights" is fundamentally at odds with court interpretation of other legislation. The Supreme Court will doubtless wish to set standards that it will follow in implementing the intent of Congress with regard to "presum-

ed correctness."

8. The ruling of the Tax Court in this case sets up a double standard for the deductability of travel expenses for professional activities, granting it capriciously to some professions but not to others. If allowed to stand this ruling will have a wide-ranging social impact. The question is raised as to whether such a standard, imposed solely for the administrative convenience of the IRS and clearly never the intent of any Congressional legislation, constitutes de facto legislation by the Executive Branch.

9. The ruling of the lower courts presents a question of whether the IRS is allowed under law to discriminate against a particular profession, artists in the particular example but not by its nature limited to that one profession,

extending beyond the particular taxpayer in this case. As a result of the precedent of discrimination against art and artists that it establishes; all artists in the United States will be placed at a particular disadvantage with respect to the Tax Code. The Supreme Court will doubtless wish to give thoughtful consideration to a decision that effectively relegates over 90% of the professional graphic artists in the United States to "hobbiest" status and deprives them, contrary to the intent of Congress, of the benefits under law readily accorded other, similar, business and professional activities.

10. A question is raised as to whether the Appeals Court can invoke a different basis for affirming a decision of the Tax Court than the basis on which the Tax Court originally stated the

opinion. A question is raised as to the legality of such invocation which the Supreme Court may wish to decide.

11. The question of thoroughness in the court system is raised. Specifically, can any court system maintain public respect if it blandly ignores the uncontested facts of a case, makes numerous factual errors of substance; and bases its fundamental decisional processes on the personal biases of the judges? A question of due process is also raised around this issue which involves the constitutional adequacy and authority of the Tax Court system itself within the Executive Branch. The question raised here is: Does the extensive power of the IRS in administration, interpretation, and adjudication of the tax code violate the concept of separation of powers?

II

Parties to the Proceeding

The formal parties to this proceeding include:

ROBERT SCOTT DUNNING,

Petitioner-Appellant

v.

COMMISSIONER OF INTERNAL REVENUE,

Respondent-Appellee

— III

Table of Contents

I. Questions Presented..... 1.

II. Parties to the Dispute..... 9.

III. Table of Contents..... 10.

IV. Reference to Reports..... 11.

V. Grounds Invoked..... 12.

VI. Constitutional Provisions..... 13.

VII. Concise Statement of the Case. 14.

VIII. Importance of the Case..... 27.

IX. Appendix..... 30.

IV

Reference to Reports

No unofficial documents relating to this case have been made public although the IRS doubtless has many such documents. A Freedom of Information/Privacy Act request to the IRS was sidestepped in 1978. The official documents are part of the Tax Court record and are included with that record.

V

(1) Nature of proceeding and Court jurisdiction-- This case is brought under the Internal Revenue Code of 1954 (26 U.S.C.) and in particular, Sections 162 and 183 of that code. The jurisdiction of the Federal Court system arises from Article XVI of the Constitution granting to Congress the right tax income and from

Article III Section 2 which grants jurisdiction to the federal courts in disputes arising from the tax laws enacted by the Congress.

(2) Entry of judgment-- The Appeals Court Judgment in this case was entered by the Appeals Court for the Fourth Circuit on October 20, 1988. A petition for rehearing with a suggestion for EN Bank review was denied and filed by the Clerk of that Court on November 22, 1988. A Notice of Appeal was filed by mail on December 9, 1988 in the Court of Appeals for the Fourth Circuit in Richmond, Virginia.

(3) Statutory provision-- The statutory provision believed to confer jurisdiction on the Supreme Court in this case is believed to be in Article III Section 2 of the Constitution of the

United States as cited above.

VI

Constitutional Provisions

The Constitutional provision under which this case is brought is believed to reside in Article XVI of the Constitution which states:

'The Congress shall have the power to lay and collect taxes on incomes, from whatever source derived, without apportionment among the several states, and without regard to any census or enumeration.'

Under this provision of the Constitution the case is brought under implementing legislation by the Congress, Specifically U.S.C. 26 sections 162 and 183 but including other legislation as ap-

plicable. Pertinent parts of Section 162 and 183 are supplied as an appendix to this document.

VII

Concise Statement of the Case

Mr. Robert Scott Dunning is a professional artist living and practicing his profession in Hampton Virginia. He also maintains a sales office and studio in nearby Virginia Beach, Virginia. Mr. Dunning is employed in the painting of portraits in oil although he is active in other media as well. He is self employed in this activity and strives to produce art which is of a technical quality suitable for museums. That is, his oil paintings, under normal museum conditions are expected to last over 400 years. The prices that Mr. Dunning charges for his

work are in keeping with their expected quality; that is, they are unusually high by normal sidewalk artist standards but are not out of keeping with the norms of serious portraiture.

As a consequence, Mr. Dunning sells his paintings infrequently. It should be noted, however, that in this respect Mr. Dunning is not out of keeping with the standards of his profession. In the United States only about 2%, or approximately four hundred professional artists out of 20,000, are able to support themselves primarily from their art. Mr. Dunning derives his main financial support by working as a research scientist for the National Aeronautics and Space Administration. In this respect he differs from most professional artists only in the discrepancy between the income that his secondary profession affords him and the

much lower income that he receives from his primary profession. Notwithstanding this, Mr. Dunning does consider that his profession as an artist is his primary profession; and to that end he strives to conduct it in a business-like manner with the intention of ultimately making a respectable living from it. He devotes far more time to his artistic career than he does to his scientific career.

In the instant case the IRS has ruled that Mr. Dunning's artistic activities are actually a hobby instead of a profession and has rejected other related deductions. This ruling was undertaken by the IRS without any investigation of the facts whatsoever. In addition this ruling was made in the face of essentially complete justification of the serious, professional nature of Mr. Dunning's business. It has been the contention of

the artist in both the Tax Court and the Appeals Court that the IRS should justify any adverse ruling by both investigation of the facts pertinent to the case and by citing pertinent sections of applicable law. This the IRS has utterly failed to do. The IRS has simply asserted, without evidence, that Mr. Dunning is not in business to make a profit and shifted the burden of proof to Mr. Dunning if he wishes to prove otherwise. Mr. Dunning has been able to substantiate all of his claims. Nevertheless, the IRS, the Tax Court and the Appeals Court have ruled against him.

The IRS rejected Mr. Dunning's legitimate and normal business expenses based solely on the incorrect assumption that Mr. Dunning is not really in business to make a profit. Mr. Dunning's contention is that the desire to make a profit

is only one of a number of criteria which are spelled out under Section 183 of the Internal Revenue Code and which should have been used; and that the desire to make a profit, although an important consideration, is in itself not the sole governing criteria for determination of the bonafide nature of a business. It is further contended that the ruling of the IRS does not adequately take into account Mr. Dunning's realistic plans for the development of his business in a fashion intended to maximize his profit. In essence, the IRS, by demanding instant profit to satisfy its unrealistic criteria for acceptance of a business activity as legitimate, has dictated the manner in which Mr. Dunning must run his business --a manner inconsistent with the inherent nature of the business. It is Mr. Dunning's contention that he is in business to make as much profit from his artistic

activities as possible in the long run and that it is his perrogative to determine the timing of his business moves and the types of business decisions which must be made to achieve that profit objective. Further, it is the contention of Mr. Dunning that his artistic activities have been conducted in a businesslike manner differing only from any other professional, business activity in the false perception by the IRS that artistic activity, which involves an element of pleasure, is somehow different and less of a business activity for that reason. It is the contention of Mr. Dunning that the IRS is in error on this point since Mr. Dunning's secondary activity, namely scientific research, is an equally pleasurable activity when properly pursued. However, in the case of scientific research, the IRS finds no difficulty on this point simply on the basis of the perceptions of its own

officials as the the relative pleasurability of the two enterprises. It is Mr. Dunning's contention that it is an unjustifiable and outrageous presumption on the part of the IRS to base its criteria for the deductablilty of business expenses on its own subjective preferences as to the degree of pleasure attached to a business.

A fundamental principle of justice in the United States is that federal agencies are required to perform the duties of their mandate in accord with the laws, rules, regulations and other requirements that the Congress establishes or which the courts lay down in their rulings; and that when an agency willfully declines to follow these requirements, the fruits of this willful disregard do not have the same standing in court as would these same results had the law been fol-

lowed. This principle finds justification in Article II of the Constitution which requires the president to "...take Care that the laws be faithfully executed,..." U.S.C. 26 Section 183(c) prescribes what must be done to determine if a business is engaged in for profit or not. Under this section the IRS and the Courts are required to give consideration to all of the pertinent factors in a case before arriving at a determination. Consideration of all pertinent factors is mandatory and the law requires that this consideration be fair. In addition this section also states that no single one of the nine factors is determinative. That is the IRS must not base its determination on one of the factors to the exclusion of the others. These requirements are separate from each other. That is:

1. **All** pertinent factors must be considered.

2. No one of the factors determines the outcome.

In issuing its Notice of Deficiency the IRS did not follow either of these directives. It based its issuance of the Notice of Deficiency on one factor only --the absence of profit in three early years of the business. It did not consider the other factors; and it did not even gather the information necessary to form conclusions about several of the factors. The Tax Court rejected the Notice of Deficiency at the beginning of the trial and never referred to it afterward. The IRS confined its written submissions concerning the case to the following items: the tax returns themselves, the "Notice of Deficiency"; and a bland statement of "agreed to facts".

None of these documents addressed compliance with the 183(c) requirements. Counsel for the IRS made no effort to establish that 183(c) had been followed. Finally, the factual errors in the answer brief filed to the Appeals Court for the Commissioner of the Revenue, written long after the Tax Court opinion was rendered, leaves no doubt whatsoever that the IRS was not and has not been in posession of the information needed to reach a conclusion with regard to 183(c). The IRS simply never followed the procedures required by law under the tax code!

It follows that the statement in the Notice of Deficiency regarding whether or not Mr. Dunning was in business to make a profit is nothing except unsupported allegation. The remaining items in dispute on the Notice of Deficiency all would have been permissible business expenditures if

Mr. Dunning prevailed on Section 183.

Finally, since there was no "presumption of correctness" in this chief issue before the Tax Court and all of the other disputed issues depended on the outcome of that issue, the entire Notice of Deficiency was improper. In law the document which the IRS characterized as a "Notice of Deficiency" was nothing more than an unsupported allegation. Nowhere in the history of jurisprudence is unsupported allegation accorded the status of being "presumptively correct".

This Appeals Court for the Washington Circuit, citing SEC v. Chenery Corp., 318 U.S. 80 (1943), has previously stressed that an "administrative agency must defend its decision in court on the same basis as it gave for the decision itself" Lanphear v. Prokop, 703 F.2d

1311, 1317, n. 39 (D.C. Cir.1983). This is so, because "[i]f an order is valid only as a determination of policy or judgement which the agency alone is authorized to make and which it has not made, a judicial judgment cannot be made to do service for an administrative judgment" *SEC* v. Chenery Corp., 318 U.S. 80, 88 (1943).

According to this precedent a court is required to base its findings on the law and the evidence before the court. It cannot simply substitute its own judicial judgment for an administrative judgement required of the IRS when the IRS fails to follow the fundamental requirements of the law under which it brings the case --the instructions in law as to how the determination is to be made. It is axiomatic that the Tax Court in sitting cannot possibly conduct an exhaustive tax

audit. In the instant case the only admissible evidence was the testimony of the taxpayer and his witness. The Tax Court recognized this fact in its bench opinion. However, it totally ignored this same fact in the body of the opinion itself. The Court at its own discretion did not elect to leave the record open for clarification or enlargement. It must only be assumed that the Court was satisfied with the evidence that was presented by the taxpayer --however incomplete that evidence might have been.

In this case the Tax Court did not believe the taxpayer and ruled against him even though all of the evidence before the court was in his favor. Taxpayer subsequently appealed the case to the Court of Appeals for the Fourth Circuit. After the filing of briefs and a detailed reply by Mr. Dunning to each and every issue raised

by the IRS, the Appeals Court rendered a two sentence affirmation of the Tax Court Decision; based, however, on grounds that the Tax Court itself had rejected. It supported a "presumption of correctness" to the IRS Statutory Notice of Deficiency. Clearly, the Appeals Court did not give the case the careful consideration normally expected of a higher court. Consequently, Mr. Dunning filed a Petition for Rehearing with a suggestion for an En Banc review with the Appeals Court which that court subsequently rejected, bringing the case to the Supreme Court in the current Appeal.

IX

Importance

This case is of considerable importance to the United States for a number of social as well as legal reasons.

The implications for art and artists boil down to a simple demand for justice under the law. Historically, the IRS has a record of discrimination against artists which cries out for rectification by the courts. Succinctly, the IRS approaches its dealings with artists from a bias which assumes that art is practiced in the United States simply as a tax dodge and that, therefore, all artists who do not make money immediately out of their art are tax cheats. This fundamental attitude precludes fair administration of the tax laws where artists are concerned. Artists, in turn, are forced to cut corners with their art in an effort to produce work fast enough and saleable enough to satisfy the IRS. Is it any surprise then that the great potential of the United States in art goes unrealized?

Legally the major question before the Court is of equal importance. That question revolves around the traditional belief in the United States that every legal entity be it a person, an institution, or a government agency, should stand before a court as equals in law. In this case, a double standard favoring a government agency stands nakedly exposed. The lower courts have simply asserted that the IRS need not bother to adhere to the tax code in the process of enforcing that code while the taxpayer must not only adhere to it; but must do so to the level of an impossible standard of proof. It should be remembered that all of the evidence in this case favored the taxpayer. The IRS never bothered to even make a case before the Court.

In the case presented here the issue of Executive versus Judicial responsibility is also of sufficient importance to justify consideration by the Supreme Court. Since the IRS clearly did not carry out its mandate in performing a tax audit, the Tax Court effectively performed the audit for the IRS. It did this even though it is simply not structured to perform this function. As a consequence, it failed miserably at getting its facts straight. In the past, the lower courts, specifically the Court of Appeals for the D.C. Circuit, have held that it is not their duty to perform mandated Executive Agency functions when the Executive Agency fails to perform that function. On the other hand, the Appeals Court for the 4'th Circuit, here repudiates that concept.

Respectfully Submitted,

Robert Scott Dunning

(Artist)

Appendix

The Appendix to this Jurisdictional Statement contains documents on larger sheets than are used in preparing this document. Accordingly, the Appendix is bound separately. The Appendix contains copies of the following documents:

1. Appeals Court, 4'th Circuit, denial of petition for rehearing.

2. Appeals Court Judgement.

3. Tax Court bench opinion.

4. Notice of Appeal filed with Appeals Court

5. Notice of Appeal filed with Tax Court

6. Copy of IRS regulations, U.S.C. 26 Section 183 as supplied to the Appeals Court by the Justice Department for the Commissioner. (Determination of intent to make a profit guidlines.)